Second Reading

The Hon. GREG PEARCE (Minister for Finance and Services, and Minister for the Illawarra) [12.10 p.m.]: I move:

That this bill be now read a second time.

The Home Building Amendment Bill 2011 has two main objectives. The first is to make a number of reforms that will remove unnecessary red tape and reduce barriers to investment in residential building work in New South Wales at the same time as maintaining adequate consumer protection. The second is to make several urgent legislative amendments, mainly as result of some recent unexpected court decisions. The outcomes of these decisions risk the Act no longer working in practice the way it was intended to operate. A healthy building sector is a key component of a strong New South Wales economy that delivers jobs and opportunities—jobs for apprentices, work for tradespeople, opportunities for small businesses and homes for New South Wales residents.

The bill is a carefully balanced package of reforms that responds to the needs of both industry and homeowners. In putting together this package, the views of key stakeholders have been taken into account and amendments made to reflect their views where appropriate. Some people may criticise the bill as they view it as going too far in one direction. At the same time others may criticise it for not going far enough. The bill strikes the right balance and provides industry with red tape reduction where possible without sacrificing fundamental consumer protections. As members would appreciate, building or renovating a home is one of the biggest expenses a homeowner will ever make. In order to protect homeowners and ensure that the industry functions efficiently, the Home Building Act regulates residential builders and tradespeople in New South Wales.

The Act's statutory warranty provisions are the linchpin of its consumer protection framework. These provisions provide implied warranties against incomplete or defective work into all contracts for residential building work. The Act also establishes the home warranty insurance scheme. The scheme provides a safety net that homeowners can access in specified circumstances where they cannot recover losses arising from incomplete or defective work from their builder or developer. The bill does not attempt to rectify all the anomalies and concerns with the operation of these schemes; nor does it address all the current issues homeowners and industry are experiencing with the regulation of residential building work in New South Wales.

Since taking office, my colleague the Minister for Fair Trading has met with key stakeholders. In so doing it became evident that a great deal of work needed to be done to the home building legislation. This is a point on which stakeholders across the board agree. There are many problems with the present regulatory framework. While some of these problems are relatively new, many of these problems have been evident for quite some time. The New South Wales Government is committed to tackling these problems. There has been a considerable amount of work done over the past few years to identify issues with the legislation and to come up with potential solutions to address these. I thank all stakeholders who have spent time providing valuable input into these processes.

The New South Wales Liberal-Nationals Government will go where others stopped short; we will make the tough decisions and see that appropriate reforms are actually made. While this bill is not an entire fix of the Home Building Act, it is an important and vital first step. The

Minister for Fair Trading has committed to undertake a broader, comprehensive stocktake of the home building legislation, starting in early 2012. I will now discuss the proposals contained in the Home Building Amendment Bill 2011. The first objective of the bill is to reform the home building legislation so that unnecessary red tape does not stymie investment in residential building in New South Wales. At the same time, appropriate protections for homeowners must be maintained.

I seek leave to incorporate the remainder of the second reading speech in *Hansard*.

Leave granted.

There is compelling evidence to support the fact that the State's residential building sector is experiencing a downturn. In August 2010, Access Economics reported that the share of home building activity has been falling since 2004. In 2010, it was at an 18-year low.

On 11 October 2011—just last week—the Master Builders Association reported that residential and commercial builders are currently facing a "worrying deterioration in business conditions".

Accordingly, the bill proposes a number of measures to cut unnecessary red tape and help stimulate this important industry.

The legislation currently provides that all residential building contracts be in writing and contain a number of requirements. This is an important consumer protection mechanism that, when complied with, helps to mitigate and resolve disputes.

However, the legislation does not differentiate between low value work and other work. This means that a contract for a small job worth $1,200 must contain the same amount of information as a contract for a job worth $120,000.

This does not make sense and places a high burden on industry.

The bill provides that the current requirements for written contracts only apply to work with a value over $5,000. To ensure· that adequate consumer protection remains, and to encourage informed decision making, the bill introduces a written quote requirement for residential building work valued between $1,001 and $5,000.

This is a sensible reform that removes unnecessary red tape while retaining proper consumer protections.

Like all things, the cost of building has been increasing over the past years: However, the legislation has not been amended to reflect this.

The legislation contains monetary thresholds above which certain requirements apply. For instance, home warranty insurance must be in place for building work valued at over $12,000. This monetary threshold has not been increased since 2004.

The bill raises the monetary threshold for mandatory home warranty insurance to $20,000. This takes into account building cost increases to date and allows for further increases in the near future.

Raising this threshold will increase competition for low-value residential building—builders

who were previously unable to undertake work of this value because they did not meet the home warranty insurance eligibility requirement will now be able to compete for this work.

When combined with not having to include a home warranty insurance premium for this work, this reform should reduce the cost of low-value residential building work for homeowners.

It should be noted that all residential building work, including work under $20,000, will still be subject to the statutory warranties and that builders will remain liable for any defective work. One of the most significant reforms in the bill is the alignment of the statutory warranty time periods with the home warranty insurance time periods.

As I mentioned earlier, statutory warranties protect homeowners from incomplete and defective residential building work by requiring builders to warrant that their work will be done to a certain standard. These 'warranties' are implied in all contracts for residential building work. Currently, a homeowner can take action for a breach of the warranties up to seven years from completion of the work no matter how minor the defect.

However, the home warranty insurance scheme warrants residential building work for six years for structural defects and two years for non-structural defects.

Overwhelmingly, stakeholders on all sides have expressed support for these warranty periods to be the same—it is too confusing and inequitable to have different warranty periods.

At present, "structural defect" is defined in clause 71 of the Home Building Regulation 2004. This definition provides that a structural defect is one that causes physical damage, or prevents, or is likely to prevent, the continued practical use of the building or any part of the building. Any component of the external walls or roof, including weatherproofing, is considered to be a structural element of the building.

"Non-structural defects" are, by default, anything that does not fall into the above definition.

The bill does not propose any change to the current definition of "structural defect". I understand that some industry groups have strong views that the current definition is too wide and requires urgent revision. Fair Trading will examine this issue in further detail, particularly in the context of a broader review of the home building legislation.

Requiring builders to warrant non-structural work for seven years is overly burdensome and impractical. Non-structural elements include painting work, kitchen cabinets and internal doors. Manufactured items like cabinets and doors may only have a 12-month manufacturer's warranty on them.

It is sensible and fair to require builders to provide warranties on this type of work for two years as is currently required under the home warranty insurance scheme.

Fair Trading complaints data supports these time periods. This data, collected by the Home Building Service since 2007, shows that over 82 per cent of complaints about structural defects are made within six years and over 80 per cent of non-structural defect complaints are made within the first two years.

Changing the statutory warranty time periods to match those for home warranty insurance will also encourage homeowners to take action to address defective work in a timely manner.

This is important, particularly in relation to non-structural defects, as over time it becomes increasingly difficult to distinguish between problems caused by fair wear and tear and problems caused by poor workmanship.

A lack of maintenance can also become a factor with the passing of time, again creating problems in determining the cause of defective building work.

I am confident that the proposed time periods—six years for structural defects and two years for non-structural defects—provide an appropriate level of consumer protection while removing an unnecessary burden on industry.

The bill provides that this amendment will commence on a date to be declared by proclamation. It is anticipated that this reform will apply to new contracts entered into after 1 February 2012.

This will allow enough time for industry and consumer groups to be made aware of the new arrangements and will also give industry associations enough time to amend their standard contracts.

This amendment is long overdue and necessary to foster a more balanced and effective market in home building. It represents genuine reform in the home building area, providing greater clarity and certainty for both consumers and industry.

The bill will amend the Act to protect homeowners who are currently uncertain of their ability to pursue their builder for faulty or incomplete work as a result of an unexpected court decision in 2010 which created a loophole in the current definition of "developer".

Prior to the 2010 Court of Appeal decision, this definition had been operating effectively. It ensured that the appropriate people and organisations were considered to be developers for the purposes of the legislation, and therefore subject to the legislative requirements for developers.

It did this by ensuring that a developer was a person or organisation that owned, or would own, four or more units in the development and that the work was done on their behalf.

One of the most important requirements in the Act for developers is that they assume the same level of responsibility for the statutory warranties as the builder. This gives a homeowner the greatest chance of recovering any losses from defective or incomplete work.

However, in May 2010, the Court of Appeal took a narrow view of the Act's definition of "developer" in its decision. It effectively found that in order for the work to be done on behalf of the developer, the developer must have been in contract with the builder.

This does not recognise that, in many arrangements entered into by developers, the party that owns the land—and on whose behalf the work is done—is not necessarily the party who enters into the contract with the builder.

The most common example of where this happens is in joint venture arrangements, where one organisation or person owns the land, and the other enters into the building contract.

Under these circumstances, if the owner of the land has to also enter into the building contract in order to be considered a developer, many homeowners risk not being able to

pursue the developer for a breach of the statutory warranties. This would severely reduce the homeowner's chances of being able to recover their losses for defective or incomplete work.

Accordingly, the Government is moving swiftly to rectify this situation for affected homeowners by amending the definition of "developer" in the Act. The revised definition of "developer" will ensure that the owner of the land who also owns, or will own, four or more of the units in the development, is considered to be a developer, regardless of whether they entered into the contract with the builder.

As a result, developers will continue to assume the same level of responsibility for the statutory warranties as they did before the Court of Appeal decision.

This amendment is to have retrospective effect, but not so as to affect any finalised litigation or claims or any claims or litigation currently underway.

The bill revises the legislation's definition of "completion" for the purposes of residential building work. The term "completion" has a very important legislative role as it triggers the commencement of the statutory warranty and home warranty insurance time periods.

Currently, the Home Building Regulation defines "completion" in relation to home warranty insurance.

However, the legislation does not provide a definition of when work is complete in relation to statutory warranties. As a result, the courts and the Consumer, Trader and Tenancy Tribunal have come to varying conclusions about when completion occurs and, therefore, when statutory warranty periods cease.

Providing a statutory definition of when completion occurs for the purposes of both statutory warranties and home warranty insurance will remove confusion, help reduce litigation and provide consistency in the legislation.

The bill provides a definition of "completion" for both these purposes, based on the regulation's definition. It also improves the current definition to better reflect the practical realities of building.

In the first instance, the bill defines "completion" as occurring in accordance with the completion provisions in the contract for residential building work.

In cases where the contract does not provide a definition of completion, or there is no contract for the work, completion occurs on the practical completion of the work.

The bill defines "practical completion" as taking place when the work is completed except for any omissions or defects that do not prevent the work from being reasonably capable of being used for its intended purpose.

The amendment to "completion" also deals with residential building work that is completed in stages by providing that separate buildings can be regarded as being practically complete in their own right prior to completion of the entire project.

This responds to concerns that, in multi building projects such as large strata complexes, an argument may be mounted that completion does not occur until every single aspect of the project is completed, even though some elements may not prevent homeowners moving in

and effectively occupying dwellings. For instance, whether or not a swimming pool in a strata complex is completed should not have a bearing on whether a unit in that complex is complete in the context of statutory warranties on the unit.

The amended definition of "completion" will commence on assent of the Act and will apply to contracts underway but not to any finalised claims or litigation or claims or litigation currently underway.

Another urgent issue addressed in this bill relates to the time limits for making claims against home warranty insurance policies, and the process that must be followed in the making of these claims.

Since 1 July 2010, the mandatory home warranty insurance scheme established by the Act has been underwritten by the Government through the New South Wales Self Insurance Corporation—an arm of New South Wales Treasury.

Between 1997 and July 2010, a number of private insurers provided home warranty insurance policies to builders consistent with the Act's requirements. These insurers wrote home warranty insurance policies on the basis that they were insuring the residential building work for a fixed period of time. Generally, the time period covered by a home warranty insurance policy is six years and six months.

However, as a result of a 2008 Supreme Court ruling and subsequent amendments to the Act in 2009, there is potential for a claim against home warranty insurance to be made at any time. In effect, this means that insurers face the real risk of unending liability for home warranty insurance claims.

As a direct result of this risk, some insurers are not releasing bank guarantees provided by builders as security against their home warranty insurance policies. At the time these securities were handed to insurers, all parties understood that they would be held for the period of insurance and then returned.

This means that builders, many of whom are small business owners, are continuing to pay interest on securities being held, at a considerable cost. This situation is also affecting the ability of these builders to take on new jobs, as their capital is tied up.

It has never been the intention of the home warranty insurance scheme for builders to be indefinitely liable for problems with their work. Neither should insurers be endlessly on risk for claims against policies. This is neither practical nor sensible.

If the proposed amendments to the Act are not made to help rectify this issue, the home building industry in this State faces yet another major problem.

To address this situation and avoid this possibility, the bill includes a number of amendments to the Act's home warranty insurance provisions. First, the bill clarifies that claims for a loss must be lodged within the period of insurance, except in cases where the loss becomes apparent in the last six months of the insurance period—in which case an additional six month claim period is allowed.

The only other exception to lodging a claim inside the insured period arises in relation to "last resort" policies. These policies indemnify the homeowner for losses that cannot be recovered from the builder due to the builder's death, disappearance, insolvency or failure to comply

with a money order of the court or the Consumer, Trader and Tenancy Tribunal.

In these situations, the bill allows homeowners to lodge a delayed claim—that is, a claim can be made outside the period of insurance—but only where the insurer has been properly notified of the loss during the period of insurance. This provision protects the rights of homeowners who cannot lodge an insurance claim during the period of insurance through no fault of their own.

The bill clarifies that in order for a homeowner to make a delayed claim they must lodge a notification in writing and diligently pursue the builder to recover the loss.

In addition to these amendments, the bill also clarifies the time limits for claims against home warranty insurance policies by revising subclause 63(3) of the regulation. This subclause deals with "related defects".

Furthermore, the bill introduces a maximum 10 year cap on when claims of any type can be made against home warranty insurance policies issued before 1 July 2010.

Put together, these amendments will remove the uncertainty around when claims can be made, and will facilitate the timely release of bank guarantees to builders.

To ensure that homeowners are not adversely affected by these amendments, the bill allows for a six month period of grace during which homeowners who have previously lodged a notification—but not in writing—will be able to lodge a written notification.

This bill reinforces the Act's consumer protection objectives and addresses an adverse 2010 Supreme Court finding by clarifying that the proportionate liability provisions of the Civil Liability Act 2002 do not apply to claims arising from a breach of statutory warranties.

As I stated earlier, the statutory warranty and home warranty insurance schemes underpin the consumer protection framework for residential building in New South Wales.

These schemes contain benefits not ordinarily available under the general law, by allowing "successor in title" homeowners to sue builders against contracts to which they are not parties, and by making developers liable to homeowners for defective work done by builders, with corresponding compensation available under home warranty insurance.

A beneficiary can seek full recovery for all losses from the builder or developer, even where a third party, such as a sub-contractor, was responsible for the defective work causing the loss.

The scheme does not prevent the builder or developer from pursuing their sub-contractors, or other third parties, under the general law to recover losses caused by sub-contractors or others.

In 2010, the Supreme Court found that the defence of proportionate liability is available to those defending claims brought under the Home Building Act's statutory warranties scheme.

The scheme of proportionate liability is established by the Civil Liability Act 2002 and applies to "apportionable" civil claims—which are claims for economic loss or damage to property caused by two or more concurrent wrongdoers that arise from a failure to take reasonable care. The liability of each wrongdoer is limited to that proportion of the loss for

which they are directly responsible.

Most residential building work is undertaken by subcontractors who work under contract to a head builder or contractor. The head builder or contractor holds a separate contract with the homeowner. Allowing builders and developers to use proportionate liability as a defence in statutory warranty claims would undermine the scheme's intent—which is for homeowners to be able to recover their total losses from their builder or developer for a breach of statutory warranty.

Under proportionate liability, if any other liable third parties are dead or insolvent, the homeowner would not be able to recover those losses, even through the home warranty insurance scheme, as home warranty insurance policies only cover builders.

Before the 2010 Supreme Court decision, it was never considered that the proportionate liability provisions of the Civil Liability Act applied to statutory warranty claims.

The bill therefore restores this situation, by specifically excluding statutory warranty claims from the proportionate liability scheme.

Currently complaints about residential building work are primarily made by the homeowner. However, since 2009, New South Wales Fair Trading has been running a pilot program where contractors can notify Fair Trading about a dispute with a homeowner over residential building work they are carrying out.

This pilot has proved to be highly successful, despite contractors facing the likelihood that an inspector who attends the site will provide the contractor with a rectification order.

Contractors working in home building generally are more aware of where to go for help. Allowing contractors to lodge complaints with Fair Trading has therefore resulted in a greater number of disputes being resolved quickly without the costs and time delays of having to proceed to a judicial process.

Accordingly, the bill formalises this pilot program by specifically providing contractors with the ability to notify New South Wales Fair Trading of a dispute with a homeowner over residential building work they are undertaking.

Other benefits for homeowners provided by the bill are the increase of the mandatory minimum amount of cover home warranty insurance policies must provide from $300,000 to $340,000. This increase reflects the rise in building costs since this threshold was last raised in 2007. This amendment updates the Act and ensures that it reflects market realities.

Additionally, the bill reduces the excess charged on home warranty insurance claims from $500 to $250. This reduces costs for homeowners involved in making a claim, but still contributes to the administrative costs borne by insurers and acts as a deterrent against vexatious or frivolous claims.

Finally, the bill closes a loophole in the legislation that can lead to abuse of the home warranty insurance scheme by effectively allowing builders or developers—rather than homeowners, as is intended—to claim on their own policies. The bill addresses this problem by providing a broader definition of corporate bodies and entities "related to" a developer or builder.

I would like to thank all the key stakeholders for the contribution they have made to the development of the bill and the support shown for the proposals. I take this opportunity to say to stakeholders, once again, the NSW Government acknowledges that this bill does not address all of their concerns and that there is a lot more work to be done in the coming months.

That said, the Home Building Amendment bill represents a solid step forward in reforming the home building regulatory framework. The New South Wales Government looks forward to continuing the process of reforming the legislation—in consultation with stakeholders—through the review next year.

I now commend the bill to the House.